No. 12954

In the United States Court of Appeals

For the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

TITLE AND TRUST COMPANY,
A CORPORATION,
Respondent.

On Petition for Review of the Decision of the Tax Court of the United States

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BRIEF FOR RESPONDENT

JURISDICTION

Jurisdiction of the above court is asserted by the Commissioner of Internal Revenue by reason of the provisions of *Section 1141 (a) of the Internal Revenue Code as amended by Section 36 of the Act of June 25, 1948.* The petition for review is from an order of the

Tax Court of the United States of which the Findings of Fact and Opinion are reported in *15 TC 510.* The jurisdictional facts are set forth in Petitioner's Brief.

QUESTIONS PRESENTED

(a) Whether or not the amount of $46,889.63 deducted as "unearned premiums" pursuant to an order of the Insurance Commissioner of Oregon made in accordance with the statutes of Oregon is a proper deduction from gross premium income and properly excluded from earned income under *Section 204 (b) (1), (4), (5) of the Internal Revenue Code.*

(b) Respondent also raises the question as to whether or not the total amount of $46,889.63 may be deducted in 1945 rather than deducted from the corporate income of 1942, 1943 and 1944 even though the order of the Insurance Commissioner of the State of Oregon was not issued until December, 1945.

STATUTES INVOLVED

Pertinent provisions of the Internal Revenue Code are set forth in this brief, and pertinent statutes of Oregon, are set forth in the Appendix, *infra.*

STATEMENT OF CASE

The facts in the case were submitted by written stipulation of facts in the Tax Court of the United States (R. 18-27). The only exhibits introduced in the case were the Respondent's income and declared value ex-

cess profits, and excess profits tax returns for the year 1945, introduced as Exhibit A. The findings made by the Tax Court are set forth in the record (R. 28-35).

Title and Trust Company is a corporation organized and existing under and by virtue of the laws of the State of Oregon, and a principal part of its business is the issuing of title insurance policies on property in the State of Oregon. The policies are single premium policies and issued in perpetuity although the liability on such policies diminishes and is ultimately extinguished with the passage of time by reason of the fact that any defects which might arise therein would ultimately be eliminated by the statute of limitations, laches and estoppel and other features of common and statutory law.

Title and Trust Company duly filed its report of income and excess profits taxes with the Collector of Internal Revenue at Portland, Oregon for the calendar year 1945, the income being determined and reported on the accrual basis of accounting. The Commissioner on examination of the return disallowed a deduction from income in the amount of $46,889.63 which had been accrued and credited in 1945 by the Title and Trust Company to a "reserve for unearned premiums" pursuant to an order of the Insurance Commissioner of the State of Oregon. The Commissioner of Internal Revenue asserted a deficiency of excess profits tax liability in the amount of $36,377.35.

Under date of December 26, 1945, the Insurance Commissioner of the State of Oregon addressed and delivered to Title and Trust Company his order in words and figures as follows, to-wit: (R. 19-22)

"STATE OF OREGON
Department of Insurance
Fire Marshall Department
December 26, 1945

"TITLE AND TRUST COMPANY
325 S. W. Fourth Avenue
Portland 4, Oregon

Dear Sirs:

"Pursuant to Section 101-136, O.C.L.A., an examination of your Company was made as of September 30, 1945 by a duly authorized examiner of this Department. Enclosed herewith is a copy of the examination report.

"On page 23 of said report attention is called to the advisability of making adequate reserve provision for unearned premiums. Study has been given by the Department towards the formulation of a reasonable, adequate, and sound rule for the determination of such a reserve. Consideration was given to the trend of your experience, premium volume, and size and types of risks underwritten. In order to make broader comparison with the requirements and procedures followed in other states as regards such reserves, the statutes of the various states were analyzed. As a consequence, in accordance with the provisions of Section 101 - 137, O.C.L.A. the following rule has been promulgated as applicable to your Company.

"1. The Title and Trust Company shall establish, segregate and maintain an unearned premium or reinsurance reserve as hereafter provided, which shall at all times and for all purposes be deemed and shall constitute unearned portions of the premiums and shall be charged as a reserve liability of your corporation in your statements; such reserve shall be cumulative and shall be established and shall consist of the following:

"(a) As at December 31, 1945 or within a period of three years thereafter an amount equal to 3% of the total gross fees and premiums received or to be received on account of policies issued during the calendar years - 1942, 1943, 1944 and 1945; and "(b) Monthly at the close of each month beginning January, 1946, 3% of the total gross fees and premiums received or to be received on account of policies written during the preceding calendar month;

"(c) After the expiration of 180 months from January 1, 1942, that portion of the unearned premium or re-insurance reserve established more than 180 months prior shall be released and shall no longer constitute part of the unearned premium or reinsurance reserve and may be used for any corporate purposes.

"2. As at December 31, 1945, the Title and Trust Company may charge against and reduce thereby the 'Title Loss Reserve' carried in the amount of $50,000.00 the total of losses paid during the four calendar years 1942, 1943, 1944, and 1945 on account of title policies issued; and monthly thereafter all such losses paid during the preceding calendar month may be similarly charged against this reserve. Provided, however, that the amount of said reserve shall never be less than an amount at least equal to the aggregate estimated amount due or to become due on account of all unpaid losses and claims upon title insurance policies of which the company has received notice nor less than the aggregate of title losses incurred during the preceding 36 months. After the expiration of 180 months from January 1, 1942, the balance in this reserve account, in excess of the aforementioned estimated amounts for claims due or accrued or 36 months aggregate losses, may be released and be available for any corporate use or purpose.

"3. Commencing January 1, 1946 the Title and Trust Company shall not issue a policy of title insurance for a single transaction, the face amount of which shall exceed an amount which is five times the capital and surplus of your Company; but nothing herein shall

prevent the Title and Trust Company from assuming the risk on a single policy jointly with another title insurance company or companies in excess of five times the Title and Trust Company's capital and surplus, provided that the total amount of such insurance shall not exceed five times the total combined capital and surplus of all such companies liable under such insurance; and provided that each such company shall not assume more than its proportionate share of the total amount at risk in accordance with the above defined maximum retention limit.

"If at any date subsequent hereto, upon review or examination as provided in the Oregon Insurance Laws, it is determined that the reserves and procedures established by the rules as promulgated above are inadequate for the safety and welfare of the policyholders and not in the best interests of the company operations, said rules will be modified as necessary; furthermore should any statute hereafter be adopted by the State of Oregon bearing on this subject, then any sections of these rules inconsistent are in conflict with said statute or statutes shall be automatically voided.

Yours very truly,
/s/ SETH B. THOMPSON
Seth B. Thompson
Insurance Commissioner"

As of the close of the taxable year ending December 31, 1945 Title and Trust Company set up on its books an account captioned "Unearned Premiums", and at that time credited to that account $46,889.63, with a corresponding debit to "Undivided Profits", the journal entry thereon being as follows:

	DEBIT	CREDIT
"Undivided Profits	$46,889.63	
Unearned Premiums		$46,889.63
To establish unearned premiums for years 1942, 1943, 1944 and 1945 in		

compliance with the ruling and demand of the Insurance Commissioner of the State Oregon, dated December 26, 1945:

1942	Premium	238,305.09	3%	7,149.15
1943	"	330,204.13	3%	9,906.12
1944	"	433,552.98	3%	13,006.59
1945	"	560,926.28	3%	16,827.77
Total				46,889.63"

In its income and declared value excess profits tax return for the taxable year ended December 31, 1945, Title and Trust Company reported a gross income of $601,664.97 consisting of the following items:

Title insurance premiums (home and branch offices)	$460,926.28	
Less: "Unearned Premiums"	46,889.63	$514,036.65
Abstract premiums (home and branch offices)		26,426.70
Commissions (trust, escrow and general)		29,991.76
Interest		13,132.36
Rents		17,312.50
Dividends		765.00
Total gross income reported		$601,664.97

From the gross income there was deducted $407,627.-31 which amount was offset by the amount of $375 and $9,523.16 representing non-taxable interest and net long-term capital gain, respectively, none of which items are in controversy, resulting in a net income to the Title and Trust Company amounting to $203,935.77 as reported on said return.

The Stipulation of Facts (R. 19-22) also refers to a

reserve for title insurance losses in the amount of $50,000 and also a deposit with the Insurance Commissioner in the amount of $100,000. The first reserve is a voluntary reserve created and accumulated by the Board of Directors of Title and Trust Company out of its earned surplus and upon which income tax had theretofore been paid. The second is a statutory deposit required by the statutes of Oregon in order to qualify for the writing of title insurance in Oregon. The references to these reserves were incorporated in the Stipulation of Facts at the request of the Commissioner and Title and Trust Company has no objection to such recitations being therein although it is the position of the Respondent here that neither the voluntary reserve nor the statutory deposit has any bearing upon the issues in the case.

Under the Stipulation of Facts the Tax Court was permitted to take judicial notice of all the statutory laws of the State of Oregon, including those specifically referred to in the Stipulation of Facts. Wherever the designation of O.C.L.A. is herein used, it refers to Oregon Compiled Laws Annotated, the official statutes of Oregon.

The Tax Court (R. 35-41) held that the Commissioner had erred in his determination that the taxpayer could not exclude from its 1945 gross income the sum of $46,889.63 as "unearned premiums" and allowed

such deduction and accordingly entered its decision finding an overpayment in excess profits tax for the calendar year 1945 in the amount of $3,713.29 (R. 42).

STATEMENT OF POINTS TO BE URGED

(a) That gross income of an insurance company (other than a life or mutual company) under *Section 204 (b) (1) of the Internal Revenue Code* includes only the amount "earned" during the taxable year from underwriting income.

(b) Underwriting income under *Section 204 (b) (4)* means premiums *earned* on insurance contracts during the taxable year, less losses incurred and expenses incurred.

(c) Premiums earned are defined in *Section 204 (b) (5) of the Internal Revenue Code,* which provides for the adjustment for unearned premiums.

(d) That the deduction for unearned premiums taken by Title and Trust Company in 1945 in the amount of $46,889.63 was justified under the provisions of *Section 204 of the Internal Revenue Code.*

(e) That the statutes of Oregon *(Section 101-137 O.C.L.A.)* contemplates in ascertaining the liabilities of an insurance company the amount of total unearned premiums on the policies in force, and authorizes the Insurance Commissioner of Oregon to make any

necessary rules, regulations or orders with respect to reserves or unearned premium liability.

(f) An order of the Insurance Commissioner of Oregon has the same force and effect as the statute, provided such an order is within the contemplation of the statute.

(g) The courts have held that a reserve for unearned premiums in the title insurance business is deductible for income tax purposes when required by state regulation, and where such reserve is withheld only for a stated period of time and then again released for corporate purposes.

(h) The entire deduction of $46,889.63 should be allowed as a deduction in 1945 as the Title and Trust Company was not required prior to that year to set up any reserve for "unearned premiums".

SUMMARY OF ARGUMENT

The Respondent in this case was required under the provisions of the Oregon statutes to comply, not only with the statutes, but with the regulations of the Insurance Commissioner, and a failure to do so could result in a suspension of its right to do business. The order of the Insurance Commissioner pursuant to the statutes of Oregon was made in the best interests of policy holders and when such an order is made and a portion of the premium reserved for a limited time and there-

after freed from restrictions after which it may be used for general corporate purposes, is a sound policy and within the scope of general insurance regulation. Such provisions are contemplated within the tax laws of the United States which permit a deduction of such a reserve for unearned premiums by insurance companies other than life or mutual. Such deduction for tax purposes is justified when such portion of the income is not to be used for a limited time for general corporate purposes.

ARGUMENT

Title and Trust Company was entitled to deduct under *Section 204 (b) of the Internal Revenue Code* the amount set up in a reserve for unearned premiums as required by the order of the Insurance Commissioner of Oregon issued pursuant to the statutes of Oregon.

Federal Statutes and Decisions

Under the Internal Revenue Code special statutory provisions are made with respect to insurance companies and divides them into three classes. Certain statutes are provided for life insurance companies. Other statutes are provided for mutual insurance companies, and a third classification is made for insurance companies other than life or mutual. The Title and Trust Company in this case is under the latter classi-

fication and is covered by the provisions of *Section 204 of the Internal Revenue Code.* The applicable provisions of *Section 204 of the Internal Revenue Code* are as follows:

"(b) DEFINITION OF INCOME, ETC. In the case of an insurance company subject to the tax imposed by this section:

(1) GROSS INCOME: 'Gross income' means the sum of (A) the combined gross amount earned during the taxable year, from investment income and from underwriting income as provided in this subsection, computed on the basis of the underwriting and investment exhibit of the annual statement approved by the National Convention of Insurance Commissioners, and (B) gain during the taxable year from the sale or other disposition of property, and (C) all other items constituting gross income under Section 22; except that in the case of a mutual fire insurance company described in paragraph (1) of subsection (a) of this section, the amount of single deposit premiums paid to such company shall not be included in gross income; * * * * * *

(4) UNDERWRITING INCOME: 'Underwriting income' means the premium earned on insurance contracts during the taxable year less losses incurred and expenses incurred;

(5) PREMIUMS EARNED: 'Premiums earned on insurance contracts during the taxable year' means an amount computed as follows:

From the amount of gross premiums written on insurance contracts during the taxable year, deduct return premiums and premiums paid for reinsurance. To the result so obtained add unearned premiums on outstanding business at the end of the preceding taxable year and deduct unearned premiums on outstanding business at the end of the taxable year.

For the purposes of this subsection, unearned premiums shall include life insurance reserves, as defined in section 201 (3) (2), pertaining to the life, burial, or funeral insurance, or annuity business of an insurance company subject to the tax imposed by this section and not qualifying as a life insurance company under section 201 (b);"

There appears to be no dispute as to the Title and Trust Company in this case being engaged in the insurance business and taxable as an insurance company under the above statute. *U. S. v. Home Title Insurance Company, 285 U. S. 191, 52 S. Ct. 319, 76 L. Ed. 695.*

Several cases have dwelt upon the question of reserves for unearned premiums and each will be discussed herein.

In *American Title Co. v. Commissioner(CCA-3)76 Fed. 2d. 332* reserves were set up under a statute of Pennsylvania. The trust company engaged in title insurance business was absorbed by a national bank. The national bank was not authorized to conduct title insurance business. A new company was formed for insurance titles and a premium of $25,000 paid by the bank in consideration of the assumption by the new company of all liability on the $36,000,000 of outstanding policies. A reserve fund was set up for the protection of policyholders as required by the laws of Pennsylvania and deducted from the gross income on a federal tax return. In that case the court held that the re-

serves were not deductible, and it will be observed also that the reserves under the Pennsylvania statute were never to be returned until the last outstanding policy of the company had died. Such a decision is quite different from the instant case where the reserve was only to be set up for a period of 180 months.

In *City Title Insurance Co. v. Commissioner (CC A-2) 152 Fed. 2d. 859* a similar ruling was made with respect to unearned premiums set up under a New York statute. The New York statute made no limitation upon time for such reserves and reserves would never be returned to the insurance company. The matter of permanent reserves seems to be the determining point in a case. In the opinion of the court reference was also made to the *American Title Co.* case, supra, and also the case of *Early v. Lawyers Title Insurance Co. (CCA-4) 132 Fed. 2d. 42,* infra. In the City Title case the deduction of reserves applied only to the years 1938 to 1941, inclusive. From the court's decision it is apparent that the New York statute was amended in 1945 to apply to unearned premium reserves and reinsurance reserves to be held for a limited time of 180 months. The court did not attempt to decide the effect of the amendment as the taxes involved were all prior to the time of the amendment.

In *Early v. Lawyers Title Insurance Co. (CCA-4) 132 Fed. 2d. 42* a deduction for unearned premiums

was made pursuant to the statute of Virginia. At the time the Virginia act went into effect in 1936, the company set up a reserve of $66,942.81 covering contracts outstanding at the date the act became effective and added thereto $29,577.86 from premiums received during the remainder of the year. The Commissioner of Internal Revenue rejected the contention that the company was entitled to a deduction of the reserve as representing unearned premiums and assessed deficiencies. Mr. Justice Parker in delivering the opinion to the court said:

"The contention of the appellant is that premiums paid for title insurance are earned when received, that there is no basis for treating any part of such premiums as unearned and that the effect of the statute of Virginia is to provide a mere solvency reserve which the company is not entitled to treat as unearned premiums. Appellant is undoubtedly correct in the position that ordinarily a premium paid for title insurance is to be treated as fully earned when received. American Title Co. v. Commissioner of Internal Revenue, 3 Cir. 76 F. 2d. 332; Huebner on Property Insurance, p. 493. And in the absence of the Virginia statute relied on by the company we should feel constrained to hold that no part of the premiums received for title insurance could be treated as 'unearned' within the meaning of the section of the Revenue Act above quoted.

"As said by the Circuit Court of Appeals of the 5th Circuit in Commissioner of Internal Revenue v. Dallas Title & Guaranty Co., 119 F. 2d. 211, 213, however, 'it is not impossible for premiums paid a title insurance company to be earned.' Unquestionably the premium collected for title insurance is not all clear profit or income to the company immediately upon its receipt. As a matter of

fact, there is a time element as well as the element of contract to be considered in connection with the risk assumed in this type of insurance as well as in other types; and if any portion of the premiums, in consideration of the time element, is given, either by law or contract, the status ordinarily accorded an unearned premium in insurance law during any portion of the period for which the risk is operative, there is no reason why it should not be treated as an 'unearned' premium within the meaning of the taxing statute during this period. We think that the Virginia statute has this effect.

"The liabiliy under a title insurance policy, which in the case of this company is shown under the law of averages to be around 6% of the premiums collected, is outstanding as a continuing liability of the company to the policyholders; and, in recognition of this fact, the Virginia statute requires that a certain portion of the premiums, 10%, be set aside and held intact for a period of time for the discharge of this liability. The sums thus set aside 'at all times and for all purposes' are, by mandate of the statute, to 'constitute unearned portions of the original premiums'. This means that they are not available to the company for its ordinary purposes, until the times limited in the statute have expired, but, until then, are held in trust for the benefit of the contract holders. If the company should in the meantime become insolvent, they would be available as unearned premiums for reinsurance of the contracts, or if not used for that purpose would belong to the contract holders. Johnson v. Button 120 Va. 339, 91 S. E. 151, 153, Lovell, v. St. Louis Mutual Life Ins. Co., 111 U. S. 264, 274, 4 S. Ct. 390, 28 L. Ed. 423,; 32 C.J. p. 1040.

"There is no reason why the legislature may not thus require the company to deal with a portion of the premiums collected, just as, in the absence of contract between the parties, it may provide how the policy is to be valued for the purpose of setting up a reserve. Cf. 32 C. J. 1017; Elder v. Bankers'

Life Ins. Co., 117 App. Div. 722, 102 N. Y. S. 702. If the statute had provided that 10% of the premiums collected should be held for the benefit of policyholders for a fixed period and should belong to the company only after it had carried the liability for that period, it would hardly be contended that this portion of the premiums was earned within the meaning of the Revenue Act until the expiration of the period; but this is precisely the effect of the Virginia statute in providing that the sums required to be placed in reserve 'shall at all times and for all purposes be considered and constitute unearned portions of the original premiums'.

"Very much in point is the decision of the Circuit Court of Appeals of the First Circuit in Massachusetts Protective Ass'n. v. United States, 1 Cir., 114 F. 2d. 304, 213. That case involved the right to deduct as unearned premiums a reserve required by law to be kept by an accident and health insurance company. In that case, as in this, there was no provision for cancellation or for return of any part of the premium to the insured. In upholding the right to deduct this reserve as unearned premiums, notwithstanding that there was no requirement that anything be returned to the policyholder, the court said:

'Congress is only interested in determining what part of a company's gross income should be treated as net income for the purposes of taxation. McCoach v. Insurance Co. of North America, 1917, 244 U. S. 585, 37 S. Ct. 709, 61 L. Ed. 1333. In general, premium income is not such, and its inclusion in gross income is only justified by the deductions allowed. See Hearings before the Committee on Ways and Means on the Revenue Act of 1918, 65th Cong., 2nd Sess., Pt. 1 (1918) 811. The additional reserve for non-cancellable health and accident policies, whether returnable to the insured or not, is not available for the use of the general purposes of the plaintiff. It is held as a liability to provide for the payment or reinsurance of specific

contingent insurance liabilities proven by experience to be a part of the cost of this particular type of insurance in the future years. * * * * As long as these reserve funds must be held to provide for expected insurance liabilities in the future on these non-cancellable health and accident policies and are not to be used for the general purposes of the company, they are not 'earned premiums' within the meaning of Congress and not includible in gross income. The test is not whether the part of the premium set aside in the reserve for non-cancellable health and accident insurance 'belongs' to the company in the event of cancellation or lapsing of the policy, but whether that amount is such a part of the company's gross income as Congress considered should be treated as net income for the purposes of taxation. McCoach v. Insurance Co. of North America, supra. We hold that it is not'."

The distinction between cases is very definitely shown. In those cases where the reserve is set up for an indefinite period of time or perpetuity, it has not been considered as a deductible item under *Section 204 of the Revenue Code.* However, in those cases where it is set up pursuant to statutory authority and for a limited period of time to cover the liability for unearned premiums and particularly to provide for any necessity of reinsurance and under a system where eventually the reserve is released for corporate purposes, the deduction of such a reserve is proper.

The court will note in the case of *Commissioner v. Dallas Title and Guaranty Co. CCA-5 119 Fed. 2d. 211,* where reserves were set up under the statutes of

Texas during a period of years and where the title insurance company had made deductions on its income tax returns for the credit made up of unearned premiums that these same funds became income when the same were released. Some of the funds involved became released to the title insurance company in 1934, and the title insurance company then took the position that the releasing of the reserve for corporate purposes did not constitute income. The court held that this much of the reserve which was returned became earned income under the satute.

See also *Utah Home Fire Insurance Company v. Commissioner 64 Fed. 2d. 763; Geyer, Cornell & Newell, Inc., 6 T. C. 96.*

After reading the above cases one can come to no other conclusion than that of finding a reserve for unearned premiums, as required in the present case, to be a deductible item and should not be included as earned income, provided such a reservation is not permanently taken away from the corporation but is only set aside in reserve for a limited time to cover any possible losses or, if necessary, for purposes of reinsurance.

State Statutes

The order of the Insurance Commissioner of Oregon, supra, and of which a copy is incorporated in the Stipulation of Facts, was premised upon authority given to the Insurance Commissioner by the statutes of Oregon. The insurance code of Oregon is embodied in *Title 101 of Oregon Compiled Laws Annotated* (herein sometimes referred to under its usual abbreviation of O. C. L. A.). The insurance code of Oregon sets out first general statutes covering the regulation of all forms of insurance. Thereafter specific statutes make additional regulations with respect to particular kinds of insurance such as life insurance, mutual companies, fraternal benefit societies, accident and health, hospital associations, marine insurance and others. The specific statutes which relate to title insurance companies are embodied in *101-1501 to 101-1505* O. C. L. A., inclusive, although such specific statutes do not have any particular bearing upon the issues arising in this case. The general insurance statutes covering all forms of insurance do have such a bearing.

The statutes of Oregon are set forth in the Appendix. Under *Section 101-105 O.C.L.A., sub-division (1)*, the Insurance Commissioner is authorized to *"issue such department rulings, instructions and orders as he may deem necessary to secure the enforcement of the provisions"* of the Act.

Under *Section 101-107 O. C. L. A., sub-divison* (7), an insurance company is permitted to transact insurance in the State of Oregon upon its compliance with the laws of this state *"and the regulations of the Insurance Department relating to such companies"*, and the payment of the necessary fees. It is further provided that the certificate to do business may be revoked on thirty days' notice by the Insurance Commissioner, or he may suspend the same temporarily if its capital is found to be impaired or if the required surplus has not been maintained, or if its transactions have been found to be in violation of the law.

The Insurance Commissioner has the authority to examine into the affairs of the company as provided in *Section 101-036 O. C. L. A.*, and has the right under *Section 101-307, O. C. L. A.* to require reserves, including a sum equal to the total unearned premiums on the policies in force, computed on a pro rata basis, and such an amount as may be necessary as a reserve to provide for the future payment of deferred and unearned claims for losses and promised benefits.

Pursuant to these statutes the Insurance Commissioner of Oregon made an examination as of September 30, 1945 of the Title and Trust Company. Such examinations are required at least once every three years under the statute. It is obvious from the order of the Insurance Commissioner that he made a very exhaustive study with respect to determination of an

adequate reserve for unearned premiums, including an analysis of the statutes of the various states, the trend and experience of the Title and Trust Company, the premium volume, and the size and types of risks underwritten, and then proceeded to establish a reserve based upon 3% of the total gross fees and premiums, and required such a reserve to be set up based upon the gross fees and premiums received from 1942 to 1945 inclusive, and to continue to make such reservation each month beginning with January of 1946. This reserve apparently was the result of an actuarial study made by the Insurance Commissioner of Oregon. This is not a permanent reserve, but is only to be held for a period of 180 months and thereafter would become released for corporate purposes. At the end of 180 months whatever is released for corporate purposes would become taxable income to the Title and Trust Company, but it is not taxable income during the year in which the reservation is made.

Title insurance, particularly in the West, is a system of evidencing titles which has practically supplanted the making of abstracts. In the last quarter of a century it has grown to a rather sizable business. As in all other parts of the country, property values materially and progressively increased, beginning with the years about 1941 and 1942. Inasmuch as the Title and Trust Company issues its policies in an amount equal to the purchase and sale price of properties, the

liability of the Title and Trust Company on its outstanding policies increased tremendously beginning with 1941. In view of this increased liability and in order to give a maximum of protection to the policyholders, the Insurance Commissioner was prompted to take such facts into consideration and order a reserve for unearned premiums.

It is asserted by the Commissioner of Internal Revenue that in order to be deductible for income tax purposes such a reserve is required to be established by statute rather than by order of the Insurance Commissioner. The Insurance Commissioner made his order under the authority given him to issue departmental rulings, instructions and orders as he may deem necessary as provided in *Section 101-105 O. C. L. A.* If such orders and regulations are not followed, the Insurance Commissioner has the right to suspend or revoke the permit of the Title and Trust Company under the provisions of *Section 101-107 O. C. L. A. Section 101-137 O. C. L. A.* gives the Insurance Commissioner specific authority in connection with the examination of insurance companies to provide for a reserve for unearned premiums. The only question remaining in connection with such an order is whether or not such a delegation of authority has the same legal effect as a statute.

After several decades of a gradual transition from substantive common law into legislative law and from

legislative law into administrative law, no one can close his eyes to the fact that administrative bodies in this decade are properly delegated with authority to make examinations, determine facts and issue rules and regulations, and if the rules and regulations are not contrary to the Constitution and statutes, they have the same force and effect as a statute enacted by the legislative body which delegated such authority.

The constitutionality of the Oregon insurance statutes has been upheld in the case of *Herbring v. Lee, 126 Or. 588, 269 Pac. 236,* and affirmed by the United States Supreme Court, *280 U. S. 111, 50 S. Ct. 49, 74 L. Ed. 217.*

Title insurance business under the statutes of Oregon has been held to be within the provisions of the general insurance laws. *Title and Trust Co. v. Wharton, 166 Or. 612, 144 Pac. 2d. 140.*

Effect of Orders and Regulations of Regulatory Bodies

In the evolution of law it has been determined that certain powers and duties may be delegated by a legislative body to an executive officer or administrative board, including the right to make such rules and regulations as may be necessary to carry into effect the

primary general laws enacted by the legislature. See *11 A. J. 945, Sec. 232* which states among other things the following:

> "Every executive officer, when called upon to act in his offical capacity, must inquire and determine whether, on the facts, the law requires him to do one thing or another, for all laws are carried into execution by officers appointed or elected for the purpose. Hence, such officers are clothed with a power which often necessarily involves in a large degree the exercise of discretion and judgment. It is definitely settled that there are no constitutional objections to the exercise of such discretion by administrative officers."

Also in *11 A. J. 949, Sec. 234,* is is pointed out that:

> "The modern tendency is to be more liberal in permitting grants of discretion to administrative bodies or officers in order to facilitate the administration of laws as the complexity of economic and governmental conditions increases."

Also in *11 A. J. 955, Sec. 240,* we find the following:

> "One of the most important limitations on the general prohibition of the delegation of legislative power to executive officers consists of a recognition of the right of the legislature under certain circumstances to delegate to executive or administrative officers and boards authority to promulgate rules and regulations. The authority to make rules and regulations to carry out an express legislative purpose or to effect the operation and enforcement of a law is not an exclusively legislative power, but is rather administrative in its nature."

Also in *11 A. J. 959, Sec. 241,* the following is stated:

> "Situations in which the various lawmaking bodies have delegated to administrative officers or boards the power to make regulations and to prescribe the necessary details to effectuate the declared policy of the law are very numerous and constantly increasing. Statutes conferring the power on executive officers to establish rules and regulations may be enacted by Congress, as well as by a state legislature; and this power may be conferred not only on executive officers, but also on administrative boards."

The Oregon Supreme Court in several decisions has upheld the right of regulatory bodies to make orders, rules and regulations, and to enforce them as to those who are regulated. In *White v. Mears, 44 Or. 215, 74 Pac. 931,* the court upheld the rights of the Commissioner for licensing sailors' boardinghouses to determine who might be licensed thereunder. In *State v. Briggs, 45 Or. 366, 77 Pac. 750, 78 Pac. 361,* the court upheld the right of a State Barber Board to prescribe qualifications of barbers. In *Stettler v. O'Hara, 69 Or. 519, 139 Pac. 743,* the court upheld the right of the Industrial Welfare Commission of the State to make an order fixing minimum wages and maximum hours of labor for women and minor workers in the City of Portland which was affirmed by the United States Supreme Court on writ of error, *243, U. S. 629, 37 S. Ct. 475, 61 L. Ed. 937.* In *State v. Terwilliger, 141 Or. 372, 11 Pac. 2d. 552, 16 Pac. 2d. 651* the court upheld the right of the Corporation Commissioner to make regulations for the sale of securities.

In *Cancilla v. Gelhar 141, Or. 184, 192, 27 Pac. 2d. 179* the court upheld the right of the State Department of Agriculture to receive and enforce delegated authority. In *Savage v. Martin, 161 Or. 660, 91 Pac. 2d. 273* the court upheld the right of the Milk Control Board to fix minimum prices and other regulatory authority with respect to the sale of milk.

We have no doubt but what the Oregon Supreme Court, if confronted with the question of the right of the Insurance Commissioner to make valid regulatory orders would be upheld as in all of the foregoing cases. The right of a state to regulate the insurance is beyond question. *29 A. J. 59, Sec. 22. 29 A. J. 61, Sec. 24* reads as follows:

> "Supervisory and Regulatory Boards of Officials. In most states, provision has been made for the creation or appointment of insurance boards, superintendents, or commissioners whose general duty and function it is to regulate and supervise the transaction of insurance business within the state so as to protect the interest of the public, to make uniform rates, to execute the insurance laws, and to see that violations of the insurance laws are properly dealt with or punished. Statutes which provide that such boards or officials shall have the power and duty to execute the insurance law of the state; to regulate and review rates of insurance; to require the submission of protective devices to tests before recognizing them as efficient factors for a lowering of fire insurance rates; to license or refuse, for cause to license insurance agents and brokers, provided statutory requirements are observed and the action of the official in such respect is not arbitrary; to serve as a statutory receiver or liquidator of insurance

companies; to approve or disapprove the amendment of the by-laws of insurance companies, have generally been upheld or recognized as constitutional and as a proper delegation of administrative or ministerial duties, rather than of legislative powers. In some cases or under some statutes, the superintendent of insurance may have the power to revoke or withhold the license or the renewal of the license of an insurance company or to examine insurance companies with reference to their assets, financial condition, and methods of doing business. The powers of a state superintendent of insurance to require that the salaries of officers of mutual insurance companies be reasonable and based upon sound business practice and to require restitution of excessive and exorbitant amounts so paid have been upheld. It has, moreover, been decided that the fact that legislative powers may have been unconstitutionally delegated to the state superintendent of insurance does not affect the validity of administrative acts performed by him without exercising legislative power or of statutes giving him administrative powers."

We also note that the United States District Court for the Western District of Texas in the case of *Petroleum Casualty Co. v. Frank Scofield, Collector of Internal Revenue,* decided August 19, 1947 (reported in CCH 1948 Vol. 5, p. 12,442, par. 9216) held that the Commissioner of Internal Revenue erred in disallowing a deduction taken by a workmen's compensation insurance company of the amount by which the taxpayer increased its reserves for unpaid claims *pursuant to an order of a state board.*

Another cogent example of a right of a legislative body to delegate authority to a board, commission or

executive officer is found in *Section 3791 of the Internal Revenue Code* under which the Commissioner of Internal Revenue is given the power to prescribe and publish all needful rules and regulations for the enforcement of the revenue laws, and such rules and regulations and the determinations of the Commissioner have been given great weight by the courts.

From the foregoing authorities it appears to be certain that the Insurance Commissioner of Oregon has full and ample authority to make the order which he promulgated on December 26, 1945, supra. The order by its own terms is not arbitrary or capricious but based upon a sound investigation of the facts and circumstances, and in the event that it is not complied with by the Title and Trust Company, we feel certain that Title and Trust Company would be deprived of its right to engage in the title insurance business in Oregon.

Unearned Premiums or Reinsurance Reserve

In connection with the order of the Insurance Commissioner, we trust that the court will not become confused in any way with the reference made to the guaranty fund deposited with the State Insurance Commissioner or the voluntary reserve accumulated by the Title and Trust Company. The guaranty fund Stipulation page 7, par. 9) of $100,000 of securities deposited with the State Insurance Commissioner is a

statutory qualification before the Title and Trust Company can engage in the business of writing title insurance in the State of Oregon. This limit of $100,000 has been in effect since 1919. The voluntary reserve of $50,000 referred to in the Stipulation of Facts (page 6, par. 8) is a reserve accumulated under the authority and direction of the Board of Directors of Title and Trust Company. The Insurance Commissioner of Oregon when he made his examination in 1945 and promulgated his order requiring an additional reserve for unearned premiums had the benefit of knowing from his own examination that the $100,000 in securities as a guaranty fund was deposited with the State, and that the company had a voluntary reserve of $50,000, and in his opinion these reserves were not sufficient to adequately cover the reserve provision for unearned premiums as the Insurance Commissioner points out in his order.

The Commissioner of Internal Revenue in the Pacific Abstract Title Company brief (page 13) dwells upon certain definitions of "premium," "unearned," and "unearned premiums." We agree with the Commissioner in saying that such terms are required to be used in their ordinary meaning. However, the term "unearned premiums" does not merely mean that it is a portion of the premium paid by a policy holder which must be returned on cancellation of the policy. It may be such portion of the premium set up in a

reserve to pay a claim for losses covered by the policy. It is ordinarily defined "as that portion of the premium which the company has not yet had time to earn." See *National Mutual Church Insurance Co. v. McGill (Ill.) 29 NE 2d. 306, 308.* As pointed out in the opinion in *Aetna Insurance Co. v Hyde, 315 Mo. 113* (cited in the Commissioner's brief, page 13), the court will discover upon reading the opinion that it definitely pointed out that the unearned premium was not limited to what was returned to the policyholder in case of cancellation. The opinion pointed out that the cost of procuring insurance was approximately 40% of the premium paid, and that the unearned premium was a liability instead of an asset, yet the company had collected unearned premium and had the cash in hand. The cost of procuring it had been paid or incurred and it was subject only to the hazard of future losses and possibly occasional cancellation.

If one analyzes carefully the title insurance business, there would be no question but what a portion of the premium represented the cost of searching the title and preparing the title insurance policy, including the expert help in such an endeavor, and would also include the usual portion of the cost of administration and supervision. In addition, however, a portion of the permium covers the risk involved. The Commissioner in his brief takes the position that the risk is of no longer duration than the issuance of the policy.

This, however, is not the case. In title insurance the risk persists through the years although it is diminished from time to time by reason of the statutes of limitations, laches and estoppel, and other common or statutory law which might terminate the right of possible claimants against the real property upon which the insurance is written. For instance, the statutes of limitations in Oregon found in *Title 1, Chapter 2, Section 1-201, et seq. O. C. L. A.,* makes various provisions for terminating the right of action, the longest of which is ten years. Some rights concerning real property would persist for a longer period of time, particularly where they involved rights of minors, insane persons or others under disability, or the sovereign state, where longer limitations apply by reason of common law or statutory exemptions from the ordinary limitations. The risk on a title insurance policy is not fixed and determined necessarily at the time of issue, but may arise at any time in the future, although the hazards thereof diminish with the passing of time. This perhaps is one of the reasons why the Insurance Commissioner felt that an order was necessary to protect policyholders on liabilities which might arise under these policies in the future as well as provide for the reinsurance of the policies in the event that the insuror for any reason went out of business, or for any other reason that would call for reinsurance. Such action on the part of the Insurance Commissioner was

undoubtedly premised upon proper foresight and a knowledge of the conditions of the community and the extent of the business written by the Company and the obligations assumed under the title insurance policies. It appears to be common knowledge that the Pacific Northwest, and particularly Oregon and Portland, have experienced substantial growth in the past decade and this fact must have been taken into consideration by the Insurance Commissioner. The fact itself would be very apparent that the title insurance companies in the area were assuming liabilities far in excess of those which had been assumed in previous years, and that the statutory reserve or deposit with the Insurance Commissioner, and in the case of Title and Trust Company, the voluntary reserve set up by its Board of Directors, appeared to the Insurance Commissioner to be insufficient to cover all of the contingencies which might arise by reason of the increased liabilities under the title insurance policies issued in the last several years. The Insurance Commissioner apparently, with wisdom and foresight, felt that the growth of the community, and the extent of liability on title insurance policies would increase rather than decrease, having in mind that all property values in the country had greatly increased, and particularly so in the Pacific Northwest. Title insurance policies are premised upon property values.

The delegation of authority to the Insurance Com-

missioner to determine how the premium should be prorated is one of the facts which the Insurance Commisioner determined by his examination and order and was not a delegation of legislative authority. The Insurance Commissioner is in a far better position to determine the pro rating, or in other words, the amount or portion of the gross fees and premiums to be set aside as a reserve for unearned premiums and for reinsurance. This he has done conservatively at the rate of 3%, and required that portion of the premiums for the years 1942 to 1945, inclusive, to be set up in the special reserve for unearned premiums, and the same procedure to be followed in subsequent years.

We do not believe it is incumbent upon the Title and Trust Company to test such an order before all the courts of Oregon before the same could be allowed as a deduction for income tax or excess profits tax purposes. Although it may be somewhat of a hardship for a corporation to have part of its earnings frozen or placed in a reserve for a period of time, and not be available for general corporate purposes, it appeals to sound reason and judgment that such a reserve as required by the State Insurance Commissioner was necessary. Eventually after the expiration of 180 months referred to in the order of the Insurance Commissioner, these amounts, or at least the unused portion theeof, will become available to the company as earnings without any restrictions as to their use for general corporate

purposes and will then become a part of the corporate income for tax purposes. It was held in the case of *Commissioner v. Dallas Title and Guaranty Co. (CCA-5) 119 Fed. 2d. 211,* that such premiums when made available for general corporate purposes at the expiration of the time limit, then become income subject to taxation by the Federal Government. See also *Commissioner v. Monarch Life Insurance Co., CCA, 114 Fed. 2d. 314.*

Also in *American Insurance Co. of Texas v. Thomas, (CCA), 146 Fed. 2d. 434,* it was pointed out that "it could hardly be maintained that a premium was entirely earned if there yet remained something to be done in later years by the insuror as a part of the consideration of its receipt," and accordingly held that it could not be characterized as *earned* premiums under *Section 204 of the Internal Revenue Code.*

A similar holding was made in *Massachusetts Protective Association v. U. S. (CCA) 114 Fed. 2d. 304.*

A good definition of reserves is given by the United States Supreme Court in the case of *Maryland Casualty Company vs. United States, 251 U. S. 342, 64 Law Ed. 297, 303,* where the court stated:

> "Reserves, as we have seen, are funds set apart as a liability in the accounts of a company to provide for the payment or reinsurance of specific,

contingent liabilities. They are held not only as security for the payment of claims, but also as funds from which payments are to be made. The amount 'reserved' in any given year may be greater than is necessary for the required purposes, or it may be less than is necesary, but the fact that it is less in one year than in the preceding year does not necessarily show either that too much or too little was reserved for the former year—it simply shows that the aggregate reserve requirement for the second year is less than the first, and this may be due to various causes. If, in this case, it were due to an overestimating of reserves for 1912, with a resulting excessive deduction for that year from gross income, *and if such excess was released to the general uses of the company and increased its free assets in 1913, to that extent it should very properly be treated as income in the year in which it became so available, for the reason that in that year, for the first time, it became free income, under the system for determining net income provided by the statute,* and the fact that it came into the possession of the company in an earlier year in which it could be used only in a special manner, which permitted it to become non-taxable, would not prevent its being considered as received in 1913 for the purposes of taxation within the meaning of the act." (Emphasis ours.)

The simple question in this case has not only been answered conclusively by the case of *Early vs. Lawyers Title Insurance Corporation, 132 Fed. 2d. 42,* but the point was actually decided prior to said decision and confirmed since.

The chronology on the cases on this particular point are as follows:

New Hampshire Fire Insurance Co. 2 T. C. 708,

which was affirmed by the Circuit Court of Appeals, First Circuit, in *Commissioner of Internal Revenue v. New Hampshire Fire Insurance Company, 146, Fed. 2d. 697.*

The above decision was followed by the decision in *Early v. Lawyers Title Insurance Corporation, CCA (4), 132 Fed. 2d. 42.*

In that case many of the same arguments were used as the Commissioner asserts in the instant case, and were answered by the court as follows:

"(6) It is argued that the term 'unearned premiums' in the taxing statute must be given its ordinary meaning. This is undoubtedly correct; but so also must the term as used in the statute of Virginia, and when given that meaning there its effect is to impress upon the portions of the premiums reserved the characteristics which bring them within the meaning of the term as used in the taxing statute.

"(7) The argument is made that to permit the deduction of the reserve set up under the Virginia statute will destroy uniformity in the application of the tax law; but uniformity is not destroyed when the factual basis to which the statute is applied is changed. The statute is applied with uniformity when unearned premiums are deducted from underwriting income; and the law of the state giving the status of unearned premiums to the portion of the premiums required to be reserved merely provides a difference in the basis of fact as to what premiums are unearned. We must look to the law of the state to deermine the nature of the interest which the company has in the por-

tions of the premiums reserved. Having determined this, we look to the federal statute to determine whether such interest is taxable thereunder. 'State law creates legal interests and rights. The federal revenue acts designate what interests or right, so created, shall be taxed'."

The above cases were followed by a suit in the United States District Court for the District of Maryland in the case of *Fidelity and Deposit Company of Maryland vs. U. S., (unreported but may be found in CCH Standard Federal Tax Reporter, 1950, Vol. 5, p. 12, 119 Par. 9106.)* In that case, the opinion points out that the plaintiff is an insurance company other than life or mutual, incorporated under the laws of the State of Maryland and was, therefore, subject to the statutes of the state pertaining to the regulations promulgated by the Maryland Insurance Commissioner. The Maryland Insurance Commissioner *by directive* issued in 1941, forbade companies doing business in the state to take credit for certain unauthorized reinsurance. The plaintiff complied with such directive and set up a reserve to cover the amount of the unauthorized reinsurance and deducted from income the amount of the reserve. In the years when this reserve for unauthorized insurance was taken down, the plaintiff paid an income tax on these amounts.

That decision was appealed to the United States Court of Appeals for the Fourth Circuit and was affirmed, *United States vs. Fidelity and Deposit Co.,*

177 Fed. 2d. 805, and a petition for rehearing denied, *178 Fed. 2d. 753.* The affirmance was premised upon the decisions in the *New Hampshire Fire Insurance Company case, supra,* and the case of *Early v. Lawyers Title Insurance Corporation, supra.*

This should conclusively answer the argument of the Commissioner that the order or directive of a regulatory body or official would not have the same effect as a statute.

We, therefore, respectfully submit that the reserve for unearned premiums set up in 1945 in the amount of $46,889.63 should be excluded from earned income of the Title and Trust Company for the year 1945.

Deduction of Full Liability in 1945

The only remaining question pertains to the full deduction in 1945 of the amount of $46,889.63 which represents the unearned premiums for the calendar years 1942, 1943, 1944 and 1945. This part of the argument is premised upon the assumption that the court will find the Title and Trust Company entitled to deduct a reserve for unearned premiums. The examination of the Insurance Commissioner of Oregon was made in 1945 and his order promulgated on December 26, 1945. Prior to December 26, 1945, there was no occasion for the Title and Trust Company to make any reservation of income for unearned premiums. During the years

1942, 1943, and 1944, the Title and Trust Company had no knowledge of any anticipated requirement that a reservation of income would be required by the Insurance Commissioner of Oregon.

Under the income tax statutes where a taxpayer is on the accrual basis, items of income are reported in full in the year in which they are earned. On the other hand, deductions or liabilities ordinarily cannot be taken or deducted until they become fixed or certain, and sometimes by an indentifiable event. The liability which results in a reservation of income for unearned premiums did not arise or become fixed until the order of the Insurance Commissioner of Oregon on December 26, 1945.

In *Lucas v. American Code Co., 280 U. S. 445, 50 S. Ct. 202, 74 L. Ed. 538, 67 A. L. R. 1010,* the United States Supreme Court held that damages for breach of a contract of employment recovered against a taxpayer accounting on the accrual basis are not deductible in the year in which the breach occurred where the amount was not determined or paid until later and which was contested and the amount was wholly unpredictable until the litigation was ultimately brought to a close.

Following this case the Supreme Court decided the case of *Lucas v. Ox Fibre Brush Co., 281 U. S. 115, 50 S. Ct. 273, 74 L. Ed. 733.* In the Ox Fibre case a

corporation granted extra compensation to its officers for services performed in prior years. The United States Supreme Court held that even though this payment was for services in prior years, it was a proper deduction in determining the taxable income of the corporation for the year in which the grant was made even though the books of the corporation were kept on an accrual basis. In its opinion the court referred to the sections of the income tax statute with respect to computing net income and stated as follows:

> "This section relates to the method of accounting; the commissioner may make the computation on a basis that does clearly reflect the income, if the method employed by the taxpayer does not. But this section does not justify the commissioner in allocating to previous years a reasonable allowance as compensation for services actually rendered, when the compensation was properly paid during the taxable year and the obligation to pay was incurred during that year and not previously. In the present instance, the expense could not be attributed to earlier years, for it was neither paid nor incurred in those years. There was no earlier accrual of liability. It was deductible in the year 1920 or not at all. Being deductible as a reasonable payment, there was no authority vested in the commissioner to disregard the actual transaction and to readjust the income on another basis which did not respond to the facts."

The accrual of a reserve to cover liability for unearned premiums is in the general category of other deductions and not entirely unlike the reasoning which is applied to debts ascertained to be worthless and

charged off. The right to take a deduction only exists in a year in which it becomes fixed or determined as pointed out by the Supreme Court in *Spring City Foundry Company v. Commissioner, 292 U. S. 182, 78 L. Ed. 1200.* This principle was further enunciated by the Supreme Court in *Security Flour Mills Company v. Commissioner, 321 U. S. 281, 64 S. Ct. 596, 88 L. Ed. 725* where the court said:

> "This legal principle has often been stated and applied. The uniform result has been denial both to Government and to the taxpayer of the privilege of allocating income or outgo to a year other than the year of actual receipt or payment, or, applying the accrual basis, the year in which the right to receive, or the obligation to pay, has become final and definite in amount."

In the case of *Commissioner v. Blaine, Mackay, Lee Co., (CCA-3) 141 Fed. 2d. 201,* the court said:

> "Under the accrual system (here in use) income is accruable in the year in which the taxpayer's right thereto becomes fixed and definite, even though it may not be actually received until a later year, while a deduction for a liability is to be accrued and taken when the liability becomes fixed certain, even though it may not be paid until a later year."

See also *Central Trust Co. v. Burnet (CCA-DC) 45 Fed. 2d. 992; Early v. Lawyers Title Ins. Corp., 132 Fed. 2d. 42, 46.*

If the Title and Trust Company in 1945 had sought to open up its returns for the year 1942 to 1944, inclusive, and sought to deduct the portion of the reserve applicable to such years, there seems to be no question but what the Commissioner of Internal Revenue would promptly disallow such deduction. Under the reasoning of the above cases, even though there had been no fundamental question arising as to the deductibility of the reserve, the Commissioner would undoubtedly disallow such a deduction purely for the reason that the amount of such deduction did not become fixed and determined until 1945 when the order was made by the Insurance Commissioner of Oregon.

CONCLUSION

In conclusion we respectfully submit that the deduction of $46,889.63 should be fully allowed in the year 1945, and that this court should affirm the decision of the Tax Court of the United States.

Respectfully submitted,

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APPENDIX

7 OREGON COMPILED LAWS ANNOTED (1940):

"*Section 101-105, OCLA, Subdivision (1).* The insurance commissioner shall have and exercise the power to enforce all the laws of the state relating to insurance, and it shall be his duty to enforce all the provisions of such laws for the public good. He shall issue such department rulings, instructions and orders as he may deem necessary to secure the enforcement of the provisions of this act, but nothing contained in this act shall be construed to prevent any company or persons affected by any order or action of the insurance commissioner from testing the validity of same in any court of competent jurisdiction."

"*Section 101-105, OCLA, Subdivision (2).* (Issuance of certificates, etc.) He shall issue all certificates and licenses under the seal of his office provided for by the terms of this act. Before granting certificates of authority to any insurance company to issue policies or make contracts of insurance in this state, the commissioner shall be satisfied by such examination as he may make, or such evidence as he may require, that such company is duly qualified under the laws of this state to transact business herein."

"*Section 101-105, OCLA, Subdivision (3).* (Furnishing of form for financial statement.) Every insurance company, doing business in the state, shall file with the commissioner on or before March 1st of each year, a financial statement for the year ending December 31st immediately preceding on [a] form furnished by the commissioner, which shall conform as nearly as may be to the form of statement from time to time adopted by the national convention of insurance commissioners, and containing such detailed exhibit of the condition and transactions of the company as the

commissioner, in such form and otherwise shall reasonably prescribe. Such statement shall be verified by the oaths of the president and secretary of the company, or in their absence by two other principal officers. The statement of a company of a foreign country shall embrace only its condition and transactions in the United States, and shall be verified by the oath of its resident manager or principal representative in the United States. In the discretion of the commissioner a penalty of ten dollars per day shall attach for delinquency in filing such statement."

"Section 101-107, OCLA, Subdivision (7). Certificate of Authority of Domestic Companies. A domestic insurance company shall be granted a certificate of authority to transact any kind or class of insurance permitted by the provisions of the insurance laws of this state and provided for in its articles of incorporation upon its compliance with the laws of this state and the regulations of the insurance department relating to such companies and the payment of the fees and charges imposed by law, which certificate may be revoked on thirty (30) days' notice by the insurance commissioner, or he may suspend same temporarily if he deems necessary or advisable. Cause for revocation or suspension of such certificate shall exist if its capital is found to be impaired or the required surplus has not been maintained or if its transactions have been found to be in violation of the law."

"Section 101-136, OCLA. (Examination into affairs of company or persons in insurance business: Appointment of examiners: Duty to produce books and papers and to facilitate examination: Report of examiners: Hearing: Inspection and publication of report: Expenses of examination.) The insurance commissioner shall, whenever he deems it advisable in the interest of policyholders or for the public good, examine into the

affairs of any insurance company, agency, corporation, partnership, person or persons engaged in or proposing to engage in the insurance business in this state, and into the affairs of any company organization under any law of this state or having an office or representative in this state, which company is engaged in or is claiming or advertising that it is engaged in organizing or receiving subscriptions for or disposing of stock of, or in any manner aiding or taking part in the formation or business of an insurance company or companies, or which is holding capital stock of one or more insurance companies for the purpose of controlling the management thereof as voting trustee or otherwise. For such purpose he may appoint as examiners one or more fair, impartial and competent persons, not officers of, nor connected with nor interested in any insurance company other than as policyholders, nor in any other company above referred to, and upon such examination, he, his deputy or any examiner authorized by him may examine under oath the officers and agents of such company or agency and all persons deemed to have material information regarding the property or business of such company or agency. Every such company or agency, its officers and agents, shall produce at the office of the company or agency where the same are kept its books and all papers in its or their possession relating to its business or affairs, and any other person may be required to produce any book or paper in his custody relevant to the examination, for the inspection of the insurance commissioner, his deputies or examiners whenever required; and the officers and agents of such company or agency shall facilitate such examination and aid the examiners in making the same so far as it is in their power to do so. Every such examiner shall make a full and true report of every examination made by him, verified by his oath, which shall comprise only facts appearing upon the books, papers, records or documents of such company or agency or ascertained from the testi-

mony sworn to of its officers or agents or other persons examined under oath concerning its affairs, and said report so verified shall be presumptive evidence in any action or proceeding in the name of the people against the company or agency, its officers or agents, of the facts stated therein. The insurance commissioner shall grant a hearing to the company or agency examined before filing any such report and before making public such report or any matters relating thereto; and may withhold any such report from public inspection for such time as he may deem proper; and if said company or agency offers no objection at said hearing, it will be an admission of acceptance; and may, after so filing, if he deems it for the interest of the public to do so, publish any such report of the result of any such examination as contained therein in one or more newspapers of the state without expense to the company or agency. Any company or association doing business in Oregon shall pay the just and legitimate expenses, including railroad fares and traveling expenses of any examination; and the commissioner shall revoke or refuse his certificate of authority to any company neglecting or refusing to pay such expenses, or neglecting or refusing to furnish any information to said commissioner. It shall be the duty of the insurance commissioner to examine every domestic insurance company at least once in three years."

"*Section 101-137, OCLA.* Examination: Reserve: Liability: (Formulating or adopting rules). In ascertaining the conditions of an insurance company under the provisions of this act, or in any examination made by the insurance commissioner, his deputy or examiner, he shall allow as assets only such investments, cash and accounts as are authorized by the laws of this state at the date of the examination, or under the laws of the state or country under which such company is organized and which investment he may approve

or reject, but unpaid premiums on policies written within three months shall be admitted as available resources. In ascertaining his liabilities, unless otherwise provided in this act, there shall be charged the capital stock, all outstanding claims, a sum equal to the total unearned premiums on the policies in force computed on a pro rata basis, and such an amount as may be found necessary as a reserve to provide for the future payment of deferred and undetermined claims for losses and promised benefits. In determining the amount of such reserve or unearned premium liability, the insurance commissioner, his deputy or examiner may formulate such rules as he may deem proper and consistent with law or he may adopt such rules as are used in other states or approved by the national convention of insurance commissioners."